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Brazil

Oilseeds and Products

Soybean Update

2005

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Report Highlights:

Post forecasts 2005/06 soybean area at 21.9 million hectares and production at 61.0 million tons, which is 2.0 million tons above the previous Post forecast. Despite a reduction in area from last year, due primarily to poor returns for the 2004/05 crop, a more normal yield is expected to lead to record production.

Includes PSD Changes: Yes
Includes Trade Matrix: No
Unscheduled Report
Brasilia [BR1]
[BR]

PS&D

| Brazil | | | | | | |
|--------------------------|---------------------------|---------------------------|---------------------------|---------------------------|---------------------------|---------------------------|
| Oilseed, Soybean (Local) | | | | | | |
| 1000 HA and 1000 Tons | | | | | | |
| | 2003 | Revised | 2004 | Estimate | 2005 | Forecast |
| | USDA Official [Old] | Post Estimate [New] | USDA Official [Old] | Post Estimate [New] | USDA Official [Old] | Post Estimate [New] |
| Market Year Begin | | 02/2004 | | 02/2005 | | 02/2006 |
| Area Planted | 21475 | 21436 | 22800 | 22800 | 23000 | 21900 |
| Area Harvested | 21475 | 21400 | 22800 | 22800 | 23000 | 21900 |
| Beginning Stocks | 3129 | 3090 | 2086 | 2219 | 1058 | 1099 |
| Production | 50500 | 50500 | 51000 | 51000 | 62000 | 61000 |
| MY Imports | 350 | 350 | 470 | 400 | 200 | 200 |
| MY Imp. from U.S. | 0 | 0 | 0 | 0 | 0 | 0 |
| MY Imp. from the EC | 0 | 0 | 0 | 0 | 0 | 0 |
| TOTAL SUPPLY | 53979 | 53940 | 53556 | 53619 | 63258 | 62299 |
| MY Exports | 19571 | 19571 | 19542 | 19500 | 22936 | 24000 |
| MY Exp. to the EC | 10200 | 10720 | 10700 | 11000 | 0 | 13000 |
| Crush Dom. Consumption | 29172 | 29000 | 29634 | 29500 | 32309 | 32500 |
| Food Use Dom. Consump. | 0 | 0 | 0 | 700 | 0 | 750 |
| Feed,Seed,Waste Dm.Cn. | 3150 | 3150 | 3322 | 2820 | 3575 | 3000 |
| TOTAL Dom. Consumption | 32322 | 32150 | 32956 | 33020 | 35884 | 36250 |
| Ending Stocks | 2086 | 2219 | 1058 | 1099 | 4438 | 2049 |
| TOTAL DISTRIBUTION | 53979 | 53940 | 53556 | 53619 | 63258 | 62299 |

Production

Post forecasts a reduction of 4 percent in planted area in 2005/06 to 21.9 million hectares but a return to a more normal yield at 2.8 tons per hectare. Production for 2005/06 is forecast at 61.0 million tons, which is 2.0 million tons above the previous Post forecast and 10 million tons greater than the 2004/05 crop. However, the Post forecast is below that of some private analysts in Brazil. For example, Safras and Mercado forecasts the crop at 63.5 million tons while Celeres foresees a crop of 63.1 million tons. Most, but by no means all, forecasters agree that area will fall with the FNP Institute forecasting area down 7 percent from last year and the Brazilian Association of Soybean Producers (Aprosoja) forecasting a 4 percent reduction. Some industry players, such as Governor Blairo Maggi, have reported that area will be down by 20 percent or more. However, post sees this dramatic area reduction forecasts as excessive and possibly meant to encourage small producers to reduce area, thus supporting prices. Nevertheless, the outlook for overall production varies much more than in recent years with forecasts ranging from 55 to 64 million tons.

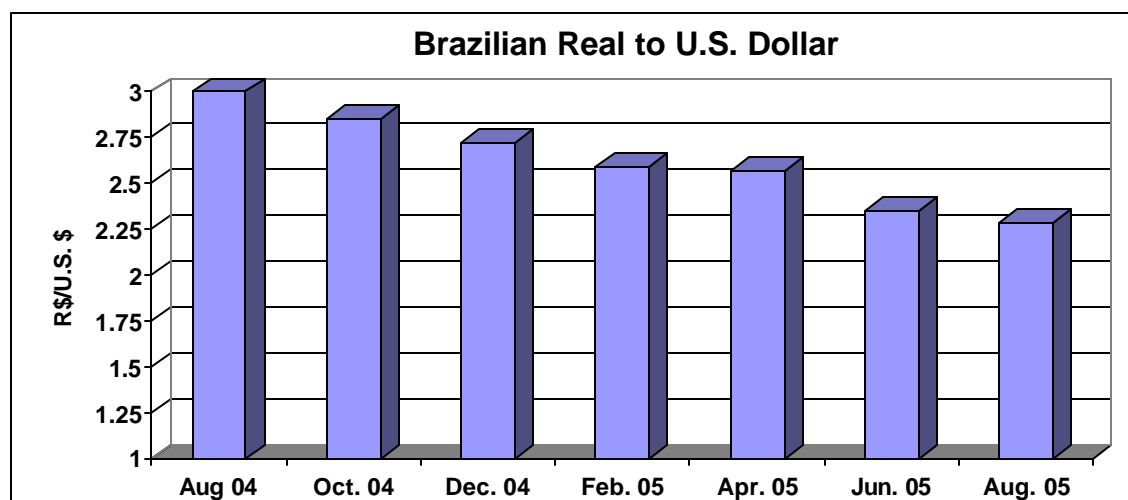
| Post Forecast Soybean Area, Yield, and Production (1000ha; tons/ha, thousand tons) | | | |
|--|-------------------------------------|--------------|-------------------|
| State | 2005/06 (Post Forecast) | | |
| | Area / % Change from 2004 | Yield | Production |
| Mato Grosso | 5,800 -5 | 3.1 | 17,980 |
| Bahia | 875 +1 | 2.9 | 2,537 |
| Goiias | 2,700 -1 | 2.9 | 7,830 |
| Mato Grosso Sul | 2,000 -2.0 | 2.9 | 5,800 |
| Sao Paulo | 750 -3 | 2.8 | 2,100 |
| Minas Gerais | 1,100 -3 | 2.6 | 2,860 |
| Parana | 3,900 -5 | 2.9 | 11,310 |
| Rio Grande do Sul | 3,450 -8 | 2.0 | 6,900 |
| Other States | 1,325 -7 | 2.8 | 3,710 |
| Total | 21,900 | 2.79 | 61,027 |

Source: Post

The Post forecast reduction in area is due to five primary factors:

- Current low commodity prices
- A strong currency
- High rate of unpaid debts
- Tight private credit
- High input costs

Ministry officials have stated that resources for production financing may be tight. The government programmed an 18 percent increase in credit with much at a subsidized rate of 8.75 percent, but all these funds may not be available due to non-payment or delayed payment on loans from the previous two harvests. However, perhaps the greatest obstacle for producers is the current exchange rate. Most producers purchased imported inputs for planting last year's summer crop at an exchange rate of R\$3.0/dollar but sold the crop at around the current rate of R\$2.30/dollar. At the current rate, dollar returns on soybean are said to be very discouraging to producers.



For the second half of the year, expectations are that the Brazilian currency (Real) will continue strong. This is due to a strong trade surplus, which is supporting the currency with a record agricultural surplus of U.S. \$20 billion for the first half of the year despite the unfavorable exchange rate for exports. These strong exports continue to inject cash into the country thereby supporting the currency. Also supporting the currency is the Central Bank's policy of maintaining a high interest rate, which currently is 19.75 percent. However, even if the Central Bank lowers the interest rate, it will likely do so very slowly as has been the Bank's tradition.

Due, in part, to this strong currency, many private analysts agree with the Ministry's forecast of reduced planted area, including MB Associados as well as Safras and Mercado, which both report that overall area will fall as should input use, given that prices received by most producers of major grain crops did not cover production costs last year. However, the reduction in area and input use should be tempered by a positive outlook in commodity prices (see chart below). In fact, those producers that have been able to hold the summer soybean and corn crops longer have obtained better prices.

| Forecast for Prices in 2005 | | | | | |
|-----------------------------------|------------------------|------------------|------------------|---------------------------|-------------------|
| | Cotton U.S.\$/Pound | Rice R\$/Sack | Corn R\$/Sack | Soybeans U.S.\$/Bushel | Wheat R\$/Sack |
| July Prices | 0.49 | 18.70 | 15.90 | 6.10 | 20.00 |
| December Prices - Forecast | 0.52 | 22.40 | 18.20 | 7.00 | 22.00 |

Source: MB Associates

Post forecasts a slight reduction in overall area including a reduction in the Center-West. This is primarily due to the difficult financial situation of many producers resulting from prices below the cost of production. Producers in the area of Primavera do Leste in Mato Grosso report that the cost of production this past year was R\$26 per sack while they sold their soybeans at only R\$22 per sack. Evidence of the reduction in planted area can be seen in lower fertilizer and seed sales to date compared to last year. The National Fertilizer Association (ANDAs) forecasts at least a 5 to 10 percent fall in fertilizer use from last year.

Post expects that the current market situation should impact planting decisions less in the Center-West than in the south since producers in the south were hit hard by drought along with low prices. In discussions with producers in the Center-West (Cerrado) region, it

appears that they are generally optimistic about prices for soybeans for the next year. This is primarily due to a more favorable outlook for soybean futures prices in Chicago as a result of concerns about the impact of the drought in the Midwest on soybean yields. Furthermore, prices for competing crops (except for corn) such as cotton and rice are also quite low. Post forecasts that soy area in the Center-West will gain minimal area at the expense of cotton and rice even though it is difficult to reduce area for these crops in the short-term due to the high investment costs. The lower costs of production for soybeans over cotton and rice is expected to favor soybeans as evidenced by a recent report by CONAB which estimates soybean profitability (as of early August costs) for the coming crop at 24 percent compared to just 4 percent for cotton.

Though Post expects a slight switch from soy area to pasture or fallow, it is believed that producers in the Center-West region are betting on a good soybean crop this year to recover from losses from the 2004/05 harvest. In a recent visit to one of the largest soybean farms in Minas Gerais, Post was informed that most producers in the region are betting on better profits from soybeans this year and are only slightly cutting back on area and inputs. Post forecasts that this reduction in area in the Center-West, particularly Mato Grosso will be on marginal cropland. Therefore, the probable reduction in fertilizer applications should be offset by the fact that producers will reduce area on the poorest soils thereby supporting overall yields.

Southern Soybean Area

There appears to be no clear consensus on the direction of planted area for southern Brazil. For example, Post cooperative contacts in RGDS believe that overall planted area in grains and oilseeds will be even with last year but that corn will take some area from soybeans. Meanwhile, Cogo Consultoria Agroecoeconomic, forecasts that due to its higher liquidity, soybean area will actually increase at the expense of corn.

| Soybean and Corn Forecast Profitability R\$ Per Hectare Based on Theoretical Early August Planting | | | | |
|---|--------------------------|---------------|---------------|--------------------|
| | Rio Grande do Sul | Parana | Goiias | Mato Grosso |
| Soybeans | | | | |
| Cost of Production | 985 | 1,208 | 1,261 | 1,281 |
| Gross Return | 1,280 | 1,485 | 1,282 | 1,282 |
| Profitability | 30% | 23% | 2% | 0% |
| Corn | | | | |
| Cost of Production | 1,391 | 1,285 | 1,493 | 1,367 |
| Gross Return | 1,800 | 1,925 | 1,610 | 1,300 |
| Profitability | 29% | 50% | 6% | -5% |

Source: Instituto FNP

Post forecasts that in the states of Parana, Santa Catarina, and Rio Grande do Sul, there will be a switch in area from soybeans to corn. The actual acreage amount may be limited to just 5 percent of soybean area. The soy/corn price spread continues to strongly favor corn and Post believes corn prices will increase in Brazil over the next several months for the following reasons:

- The government is maintaining a very strict policy on importation of biotech corn from Argentina. While 400,000 tons are being imported into the Northeast, further imports are not permitted. With the small summer and winter corn crops, imports are needed to maintain price stability. It is important to note that the price of imported Argentine corn has traditionally been a market reference price as domestic prices only rise to the point where imports are possible. However, with imports not allowed, this reference maximum price is no longer relevant.
- Demand from the pork and poultry industries remain very strong with exports unaffected by the strong currency.
- Government sales of corn stocks at very low prices are currently stabilizing prices. However, these stocks are dwindling quickly and once government auctions slow, prices should react.
- Strong producer selling of remaining summer supplies in the south and winter corn from Mato Grosso is also supporting prices. However, as this producer selling slows over the next few months, prices should increase significantly. Meanwhile, growers are holding soybean supplies in hopes of better prices. Therefore, once this grain is released, soybean prices for the domestic market should fall, or at least not increase to the magnitude of corn prices.

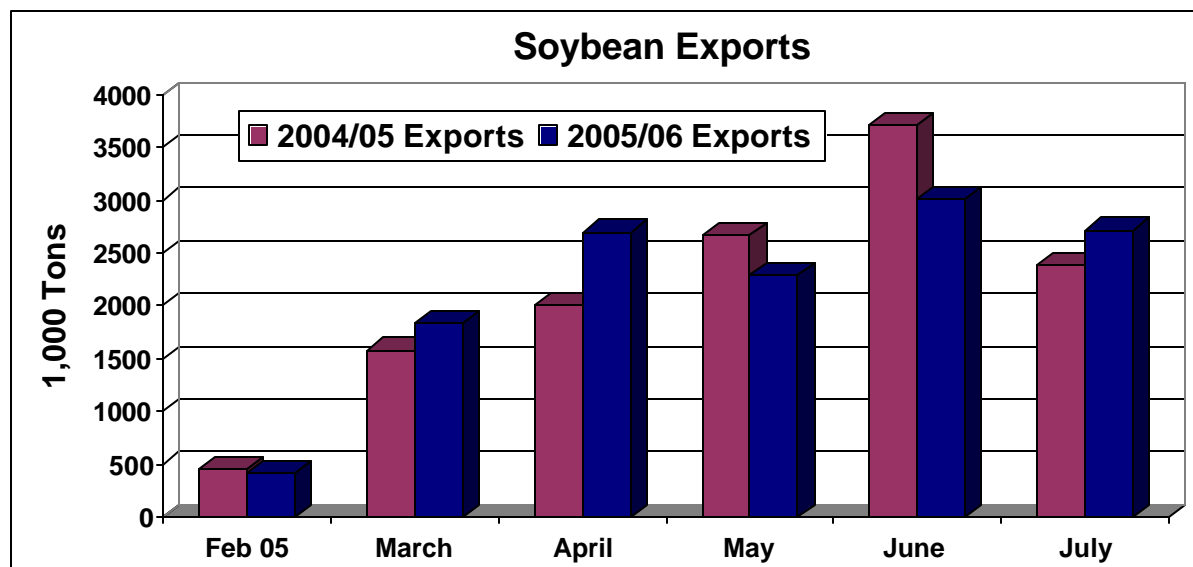
In summary, while prices for corn are expected to remain stable over the next 30 days, due to the winter harvest and producer selling, market conditions are expected to change and prices should be higher by summer crop planting. This should further decrease the soy/corn spread and confirm the 5 to 10 percent area switch in the south.

As discussed above, Post feels that there should be a small decrease in national planted area to soybeans. However, Post also observes that many analysts are under forecasting yields. Post expects a slight reduction in fertilizer applications in some regions but this should be offset by more normal weather, a continued increase in the use of high-yielding soybean varieties, and better control of soybean rust. Yields in 2002/03 were slightly above 2.8 tons per hectare with the yields impacted that year by soybean rust. Furthermore, yields in 2000/01 reached 2.84 tons per hectare and since then there has been improvement in varieties. Therefore, Post conservatively forecasts a national yield of 2.79 tons per hectare, which is just slightly above the 5-year average, which includes two crops that were severely impacted by drought. With less planted area, forecast at 21.9 million hectares, this gives overall production of roughly 61.0 million tons, which is 2.0 million tons above the previous Post forecast.

Trade

Post forecasts soybean exports for the period from February 2006 to March 2007 at 24.0 million tons, which is 4.5 million tons greater than forecast exports this year. The higher forecast is primarily due to greater supply as a result of the increase in production of 2.0 million tons over the previous Post forecast as well as less export competition from the United States.

Total exports for 2004/05 reached 19.3 million tons, down just 730,000 tons from the previous year. Post forecasts marketing year 2005/06 (beginning in Feb. 2005) exports at 19.5 million tons, compared to the previous Post forecast of 19.2 million tons. Exports for the first 6 months of the marketing year are nearly identical to shipments last year. Though the currency is much stronger this year, exports thus far in the year have been unaffected by significant delays at the ports. Additionally, shipments have been uninterrupted to China while last year there were significant difficulties. Sales over the next few months are expected to remain strong as concerns over the U.S. crop, and related strong futures prices, make Brazilian soybeans more competitive.



Biotechnology

Monsanto announced in June that it will charge a royalty fee of R\$0.88 per kilo of certified seed but this was subsequently lowered to R\$0.77 per kilo at the request of the Brazilian Seed Producers Association (ABRASEM, in Portuguese). Nevertheless, given the current poor financial situation of many producers, some producer organizations are pressing Monsanto to delay the collection of full royalty fees on certified biotech soybean seed until 2006/07. Producers in Rio Grande do Sul argue that poor crops the past two years have cut returns and suggest that this coming year the fee should be based on two percent of the value of production. According to the Rio Grande do Sul Seed Producers Association this would lead to total payments to Monsanto of R\$8.4 million instead of the current projection of R\$17.7 million.